



## **Strategic FM Procurement: an issue of aligning services to business needs**

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## Strategic FM Procurement: an issue of aligning services to business needs.

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### ABSTRACT

**Purpose** – To illustrate the interdependence between business need and strategic decision on facilities management (FM) procurement model. This interdependence underpins the reason behind strategic decision on FM procurement. It would assist decision makers on FM services procurement that fulfills business needs and enriches business outcomes.

**Design/methodology/approach** – By a systematic review of FM-related literature, this research structures and investigates on three aspects of this interdependence between business delivery and FM services: 1. What characteristics of core business impact on FM service and provision? 2. What are the interconnections between business support and FM procurement decisions? and 3. What are the available FM services procurement options?

**Findings** – There are four types of core business characteristics that impacts on FM services and provision based on the *degree of criticality* to business continuity. Each type of core business needs determines decisions on FM procurement which vary with the *degree of collaborative relationship* between decision makers and FM service providers. The degree of collaborative relationship encapsulates *the number of communication channels, stakeholders' involved, direction of data transfer and nature of data exchange*. Consequently, the collaboration among parties involved determines the form and format of FM procurement model.

**Research limitations/implications** – This approach can be used as a decision-making framework for management to assess its FM services procurement decision, and to justify the needs of FM provision and services. On the other hand, an FM organization can use it as a self-evaluation tool to evaluate its FM procurement and degree of alignment of its current offering with core business needs. As the approach is based on a limited number of detailed case studies, further empirical verification of various types of organizations and contexts will be needed.

**Originality/value** Although this proposed approach is formulated within the context of FM procurement, its applications can be applied to other organizational support functions, for instance human resource (HR), information technology (IT) and finance services.

**Keywords:** Business need, Business support, Alignment, Strategic FM procurement, FM procurement strategy.

### 1. INTRODUCTION

Michael Porter's organizational value chain (Porter, 1980) divides business units into two building blocks: (1) Primary activities are organizational core competencies that possess the competitive advantage to surpass their business competitors. They create the monetary value to the organization.

(2) Support activities are an organizational non-core competency that supports the operation and production of the primary activities. They create the non-monetary value. The only monetary value contribution is cost reduction.

FM is the integration of processes within an organization to maintain and develop the agreed services which support and improve the effectiveness of its primary activities, (CEN, 2010). Regarded as a non-organizational core competence and a non-critical function, FM activities are likely to be performed and contracted out to third parties who hold specialized knowledge and expertise. This managerial perspective confines the boundary of FM's scope, role and function as their added value creation is only limited to achieving prescribed service levels at the lowest cost. As a result, other potential added value aspects from FM are being neglected.

This research intends to unfold the unarticulated notions of added value of FM. A better understanding of added value opportunities from FM services provision will broaden existing corporate management's perceptions of its abilities and utilities. The research deployed the asset specificity theory as an overarching framework by comparative analysis of FM literature with empirical findings from FM practices in selected case studies. The practical implication of this research is to illustrate the interdependence between business need and strategic decision on FM procurement. This interdependence underpins the reason behind strategic decision on FM procurement. It helps corporate management to make the decision on which FM functions should be outsourced and/or kept in-house, and under what circumstances the most effective and efficient collaborative relationship between FM organizations and their clients can be achieved.

## 2. OVERVIEW OF ASSET SPECIFICITY

Coase (1937) raised the question of what drives organizational form, and largely developed the theoretical framework referred to as transaction cost economy (TCE). The essence is that "economizing on transaction costs would determine the organization of economic activity, and the division of activity between firms and markets" (Milgrom and Roberts, 1992, p. 51). He proposed that a firm will replace the market provision when the costs of transacting within the firm are less than the costs of transacting through the market. The manner in which a transaction is organized depends on particular attributes of the transaction. Most TCE researchers (Williamson, 1979, 1981, 1985, 1996) discuss three critical transaction attributes: (1) Asset specificity; (2) Uncertainty; and (3) Frequency. Asset specificity is argued to be the most important factor in determining the choice of governance, namely hierarchy or market.

Asset specificity was described as the 'specialized ability' by Marshall (1949, p. 172) in the transaction relationship that is required for particular functions and requirements. Williamson (1985, p. 95) defines asset specificity as 'the degree to which an asset can be redeployed to alternative uses by alternative users without sacrifice of productive value'. TCE suggests that asset-specific investments should only be deployed on the expectation of substantial cost savings and/or value-adding advantages, but it also posits that asset specificity increases the hazards of opportunism and the transaction costs necessary to safeguard against the risk of opportunistic expropriation (Heide and Stump 1995; Parkhe 1993).

Based on the level of asset specificity, firms will formulate an appropriate governance structure, with inter-firm relationship performance expected to be maximised when opportunistic behavior incentivized by asset specificity is reduced (David and Han 2004; Lui et al. 2009; Rindfleisch and Heide 1997). De Vita et al. (2011) explain the usage of asset specificity as a core concept of TCE (also commonly referred to as transaction cost theory, TCT), which is still seen as the dominant theoretical framework for studying organizational boundary choices (Geyskens et al. 2006). In particular, asset specificity has become a key construct in research into make-or-buy decisions

(Espino-Rodríguez et al. 2008) and the performance of buyer–supplier relationships (Artz 1999; Haugland 1999; Heide and Miner 1992; Heide and Stump 1995; Lui et al. 2006, 2009).

## 2.1 Seven Dimensions of Asset Specificity

Asset specificity consists of seven dimensions: Their characteristics are described below.

**Human asset specificity** refers to the degree to which skills, knowledge and experience of a firm's personnel are specific to the requirements of dealing with other firms (Zaheer and Venkatraman, 1995). It encompasses any unique knowledge or skills that suppliers develop through training, and represents specialized know-how or experience specific to a particular employer/employee relationship (Lamminmaki, 2005).

**Site asset specificity** refers to the transaction relationship when the buyer and the supplier are in close proximity to a buyer or seller in terms of site, location and facility production. This aims to reduce inventory and other related processing costs. (Joskow, 1988; Lamminmaki, 2005; Morill and Morill 2003; Williamson, 1983).

**Physical asset specificity** refers to investments in physical assets that are tailored to a specific transaction and have few alternative uses, owing to their specific characteristics (Joskow 1988; Morill and Morill 2003). Comparing with human asset specificity it is more tangible to measure and assess the uniqueness of equipment and tools required by the supplier for the purpose of the transactional relationship (Klein and Roth 1990; Heide and Stump 1995; Walker and Poppo 1991).

**Dedicated asset specificity** refers to assets that are of general purpose as opposed to specialized uses (physical asset specificity), but which have been made for a particular transactional agreement that is likely to entail a long-term relationship (De Vita *et al.* 2011). Lamminmaki (2005) provides an example from the hotel industry as a hotel might expand its facilities on the assumption that delegates from a neighboring conference venue will use its facilities.

**Brand asset specificity** refers to organizational reputation. For instance, a supplier could find himself in a position enabling him to directly or indirectly cause damage to the client's reputation (Gatignon and Anderson 1988; Lamminmaki 2005; Lohtia et al. 1994). A buyer-supplier relationship involving activities which have a direct and great impact on the overall business performance and brand reputation could be considered as high brand asset specificity.

**Temporal asset specificity** refers to the matching of timing and co-ordination required by a transactional relationship between a buyer and a supplier. This concerns investment where timing and coordination of activities is critical, i.e. timing and coordination represent the high temporal asset (Lamminmaki 2005). An unsuccessful coordinating will lead to the failure of business outcome.

**Procedural asset specificity** refers to organizational business processes, routines and workflows (De Vita *et al.* 2011). This type of asset specificity is common in service industry. The transactional relationship will be high when buyers heavily rely on suppliers who customize their work process to a particular buyer's business process. It is difficult to replace once created or to redeploy without value reduction.

These seven dimensions of asset specificity form distinct and interrelated, rather than substituted and isolated, dimensions of the construct. The interconnection of the asset specificity dimensions indicates that simply investigating one dimension of the construct may be inadequate. For example, physical, procedural and site specificity involve the allocation of staff with specialist knowledge and skills or specially trained personnel to perform the activity i.e. human asset specificity (Lamminmaki 2005). Site specificity may be highly correlated to temporal asset specificity to ensure smooth and zero downtime delivery of services, which enables the brand asset specificity in

service industries where just-in-time delivery is a core activity of business operations. Similarly, temporal specificity may require the supplier and/or the buyer to assign specialized staff (human asset specificity) and customize existing operating process (procedural asset specificity) to meet the needs and requirements of the transactional relationship.

### 3. VALUE ADDED BY FM IN RELATION TO ASSET SPECIFICITY

The key supportive role of FM to the core business involves managing facilities resources, support services and the working environment for both the short and long term (Then and Tan 2013, Chotipanich 2004; Tay and Oui 2001). In order to deliver facilities services or facilities products and/or add value to the client organization, FM needs to align the organization's primary processes with facilities processes (CEN 2010, Then, 2003; Then and Tan, 2006). In order to align FM processes closely with its core business processes, FM organizations have to be involved in the strategic decision making process. However, FM is generally perceived among clients, customers and end-users as a back office function. This paper discusses asset specificity from FM activities and their performance that add value to the core business and surroundings, based on FM-related specialized abilities. The nature of the transactions between an FM organization (supply side) with its client (demand side) can be explained by asset specificity which describes the extent to which a given FM product or service is tailored to a client's specific needs and requirements based on their "*specialized abilities*" in terms of the nature of the core business, customer type, primary activities, business needs and requirements.

This paper proposes that the degree of asset specificity of FM services can also be implied as the degree of value added undertaken by an FM service provider to its host organization. The added value perceived by its host organization will be reflected in the adopted structure of FM's scope, role and function within the organization. The appropriate FM provision is characterized by varying degrees of asset specificity depending on the complexity and customization of the FM products offering in terms of workplace solutions, service delivering, managerial skill sets, labor and workforce.

The following presents seven types of asset specificity from FM-related specialized abilities that add value to the core business and surroundings:

- **Human asset specificity** represents specialized know-how or experience specific to particular FM organizations and their clients. It is acquired from both the prior work experience and emerging knowhow from performing a current job. It has limited relevance to other task situations and organizations.
- **Site asset specificity** refers to reducing the commuting distance between the demand side and supply side. The supply side encompasses FM organizations from both in-house and service providers and sources of facilities and facility services. The proximity between both sides creates the cost advantage through the reduction of redundant information processes, transaction cost and real estate cost.
- **Physical asset specificity** can be seen as customized infrastructure, workspaces and FM services. FM organizations play a critical role to its client's core business because their bespoke facility services and infrastructure are critical to the organization's performance and business outcomes in terms of increasing customer satisfaction, employee productivity and organization's revenue.
- **Dedicated asset specificity** is contrary to physical asset specificity in that FM organizations offer a range of standardized FM services and provision. Organizations can benefit from dedicated asset specificity by optimizing economies of scope and scale. Economies of scale are

offered by large investments in capacity which, although they are not bespoke, present problems in finding another buyer who wants to use the spare capacity (Finch, 1996). Economies of scope are offered by FM operations and management systems that encompass an entire FM supply chain, for instance the concept of TFM.

- **Brand asset specificity** refers to FM practices that support the corporate culture, enhance the corporate reputation and help organizations to attract and retain potential talented employees. This brand asset specificity is aligned with the current organizational cultural strategy aimed at increasing the organizational capacity and capability..
- **Temporal asset specificity** refers to added values created from time-sensitive FM applicability. It can be practiced in FM services and provision by just-in-time inventory practice that helps corporation to avoid and minimize the cost of inventory holding.
- **Procedural asset specificity** includes systems and practice of the client's organization for which the FM organization's processes and practices must integrate with their client's work processes.

#### 4. EXEMPLARY CASE STUDIES

The case studies selection criterion is to maximize variations that aim to highlight the potential applications and capability of the asset specificity for the various contexts and circumstances in organizations from public, private and state-owned sectors. The data collection was carried out by semi-structured interviews with stakeholders from both the demand side and supply side spanning strategic, tactical and operational levels. The main interview theme focuses on an aligning of perception from the demand side (client, business units and end users) and implementation from the supply side (external service providers) on added value from FM services and provision to core business and surroundings, through their FM procurement strategy.

##### 4.1 LEGO

LEGO is a Danish toys manufacturing company. LEGO wants its FM operation and practices to align with its corporate culture (i.e. human asset specificity). Most of the FM products are performed by in-house staff. FM department wants to deliver its FM products in a timely manner according to its client's, customers' and end users' needs with the least costs of inventory holding (i.e. temporal asset specificity). LEGO's ownership strategy is to lease real estate for not more than 10 years because of flexibility and uncertainties of market price. The flexibility of FM product can be also classified as temporal asset specificity from the FM organization to LEGO.

##### 4.2 Mærsk

Mærsk's core business is oil and gas exploration, retail store, container tower, container shipping and related businesses. Mærsk aims to focus only on its core business and assigns the support service tasks to professional service providers. Mærsk's real estate and FM strategy is to rent all buildings and outsourcing to capable FM providers to perform Mærsk's facility support services. Mærsk requires the stripped down and standardized FM services that support the operation of primary activities with a low rate of operational downtime. Mærsk has adopted a Total FM (TFM) sourcing arrangement by contracting out FM support services to a single FM provider (Johnson Controls Inc. (JCI)) at a global level. JCI's specialized ability is dedicated asset specificity because Mærsk's core business benefits from economies of scope and scale of a service provider who possesses the managerial capacity and operational capability.

##### 4.3 PTT Public Company Limited (PTT)

PTT is a Thai state-owned energy company. Previously, subsidiary companies of PTT rented office spaces separately around Bangkok and contracted out FM services individually. To consolidate the amount of workplace and standardized FM practices among its subsidiary companies and to reduce the FM operating and administrative costs, ENCO was established as a semi-autonomous company responsible for managing FM services and provision for the new office campus. One single centralized location is considered as site asset specificity to PTT's subsidiary companies. At the initial phase of organizational re-structuring, there was a shortage of FM knowledge, expertise and workforces, so ENCO heavily relies on external FM professional skills, both managerial expertise and technical skills from its main service provider; CBRE. ENCO currently needs to employ human asset specificity from CBRE. This office campus is intended to be a multi-tenants office for subsidiaries companies by sharing the common area and FM services. PTT can benefit from economies of scope and scale of shared service which can be classified as dedicated asset specificity.

#### **4.4 PTTEP (PTT Exploration and Production)**

PTT Exploration and Production (PTTEP) is a subsidiary of PTT. PTTEP had experienced leaks of confidential information from temporary FM workers causing security problems and loss of business opportunities. PTTEP thus relies on trusted employees— especially blue collar workers at the operational level who have access to all areas. The challenge in managing the FM workforce is a high rate of FM staff turnover because the operational FM job comprises only routine tasks, with low pay, fringe benefits and job security. In order to decrease the churn rate of FM employees, attracting and retaining trusted and skilled workers and increasing employee loyalty are critical. The FM department initiated collaboration between PTT's HR and service providers. PTTEP offers above average fringe benefits to FM blue collar workers and treats them as internal PTTEP's employees. In this respect, the requirements of a given type of FM workforce are considered as a human asset specificity. In cases of contractor termination and vendor switching, PTTEP will continue to hire the incumbent FM staffs but selects the new service providers to supervise them. This collaborative initiative can also be seen as brand asset specificity. It increases PTT's reputation as PTTEP's host organization remains one of the most attractive workplaces in Thailand.

#### **4.5 Hong Kong Science and Technology Parks (HKSTP)**

HKSTPC (Hong Kong Science and Technology Parks Corporation) manages and provides purpose-built R&D office spaces, advanced laboratories and technical support services for technology-oriented start-up companies and multinational corporations. This brand asset specificity enables and brands Hong Kong's position as a regional technology hub. The single office campus is dedicated as site asset specificity to tenants. FM processes are embedded with tenant's activities because technology-savvy tenants demand the most reliable FM services and provisions to ensure reliably delivery of their operations and activities. This arrangement can be considered as procedural asset specificity. In order to manage and organize the world class facility hub, the FM organization in collaboration with a service provider (ISS) initiated a facilities manager trainee program that aims to develop and cultivate FM practitioners who have the appropriate FM knowledge ranging from technical to managerial skills. The exchange of knowledge between internal FM knowledge and external FM provider operational expertise can be perceived as human asset specificity.

#### **4.6 Dutch central government**

The Dutch central government had to reduce operating costs and staffing levels in thirteen government departments. Each of them had its own FM organization, provision arrangement and practices. It caused redundancy and non-standardized FM products and practices within the Dutch state agency. The Dutch central government commenced an organizational merger which led to the consolidation from thirteen business units into one centralized unit. FM as a support function from

each public department was amalgamated into one single department and reports directly to the central department. This can be a source of added value by service standardization, consolidation of common functions across the multiple organizations, economies of scale and scope, reduction of the redundant information processes and transaction cost reduction. This demonstrates a case based on dedicated asset specificity.

#### 4.7 Thai central government

Previously 35 state agencies rented and leased their own workplaces spreading across Bangkok greater area. The Thai central government then initiated an office campus project as a state property management project by offering office space to government agencies at the right budget. The Thai central government established Dhanarak Asset Development (DAD) as the independent subsidiary company of the central government for managing FM provision and services for the government office complex. This centralized location can be considered as site asset specificity. DAD can increase its negotiation power for procurement of FM services. The Thai government can benefit from economies of scale and scope which is based on dedicated asset specificity.

### 5 DISCUSSION

Chotipanich (2004) pinpoints two main basic factors that impact the choices of facilities and services needs in organizational decision making process: first, *internal factors*, such as organizational characteristics, facilities features and business sector and second, *external factors*, such as economic, social, environment, legislation and regulation, FM market context and local culture and context. These factors define the characteristics of decision making behavior and the primary stakeholders who are involved in the decision making process.

Asset specificity theory adds another external determinant factor that justifies FM's scope, role and function in the given organization: *FM-related specialized abilities*. It is considered as the above the line contribution or offering from FM organizations. It can be connoted as the value added from FM provisions and services to the organization's core business.

This paper formulates *four value adding positions* and their associated characteristics of FM-related specialized abilities that add value to the core business and surroundings. Each of them has a particular characteristic of collaborative relationships between the FM organizations and their stakeholders. This also explains the rationales and actions behind the strategic decision making on the *what*, and *why* of outsourced FM support functions. In order to deliver the right specialized abilities to the demand side this paper argues that each type of collaborative relationship requires different groups of primary stakeholders as follows:

- FM-related specialized abilities that *support the operation of the organizational primary activities* running more effectively and efficiently with a cost advantage. This type of FM-related specialized ability is relevant to *dedicated asset specificity* that corporations could benefit from achieving economies of scope and/or scale. FM organizations need to collaborate with *senior management* of the given organization. It is the conventional spot-market relationship with a cost-sensitive contractual agreement. However, the involvement of the FM organization is only at the operational level. FM services and provisions are required as a commodity, which has no significant difference among different FM providers.
- FM-related specialized abilities that *enable the organizational capacity and capability* with the specific organization's demands. In this category, the FM organizations and their demand side establish one-off decisions and implementations responding to current organizational demands. The FM organizations offer cutting-edge practices, performance framework, processes and managerial expertise that enable organizational productivity, business profitability, operational



efficiency and effectiveness and also end user satisfaction. This includes three asset specificities: ***brand, site and temporal asset specificity***. FM organizations need to collaborate with ***one or more of the business unit directors and senior management*** of the client's organization at the operational and tactical levels. The FM providers and their host organizations mutually share economic risks and benefits. Cost reduction still plays a key role in the decision making process.

- FM-related specialized abilities that ***ensure the operation and performance continuity of primary activities*** continuing to operate normally and without interruption. FM organizations offer FM services and provisions focusing on operational reliability and minimizing the operation downtime. Corporations rely on FM knowledge, workforce, skills and expertise that are aligned with the host organization's business processes. This covers two asset specificities: ***procedural and human asset specific***. The FM organizations need to be highly collaborative and engage with ***a board of business units' directors***, particularly production. Under this arrangement, the FM organizations and their host organizations share mutual risks, benefits, trust and a committed relationship. The FM organizations and their clients' relationships move from a spot market-driven relationship towards becoming the preferred partners. The FM working processes are embedded into the organizations' primary activities. Facilities managers play a key role from tactical to strategic levels.
- FM-related specialized abilities that ***enhance operational performance and business outcomes*** of the core business. In this category, the FM performances immediately and directly impact the end users' perceptions and satisfactions. Their service specifications are highly customized by end users' requirements in order to enhance the end users' satisfaction and productivity. Any downtimes will immediately impact on the organizational operations and outcomes. The FM organization co-creates and customizes the FM services and provision specification with all relevant stakeholders with involvement from client, business units and end users. This type of FM-related specialized ability is relevant to ***physical asset specificity*** that highly customizes infrastructure, workspace and FM services to FM's stakeholders. The FM organization needs to collaborate with the ***end users*** of the client's organization. The roles and responsibilities of FM shift away from supportive roles to becoming part of an organizational core functions. The facilities manager can engage in the client's organization's decision making process.

From the above discussions, FM-related specialized abilities involved with *procedural, human and physical asset specificities* should be kept in-house unless corporations need to find the most optimal way to fulfill their needs from the demand side with FM-related specialized abilities from external suppliers. Such corporations tend to outsource or out-task FM provision and services to external service providers who hold particular skills and expertise. Each of them requires a specific managerial approach. For example, FM activities that provide *dedicated asset specificity* with cost advantage may not need to engage in strategic decision as much as *physical asset specificity* that enhances organizational performance and outcomes. In cases when a corporate decision on FM procurement provision is made by senior management to take advantage of purely cost advantage (i.e. dedicated asset specificity), other stakeholder groups including FM organizations may be excluded from the decision making process.

## 6 CONCLUSION

The above value adding positions can also be applied to create a constructive dialogue between both demand and supply sides to converge and align FM's offerings with core business's expectations. From the supply side, FM organizations can use the proposed FM specialized abilities to develop

their capacity, capability, competency and resource to supply core business's needs and requirements. From the demand side, clients can use the proposed value adding positions to define and manipulate the role of service providers in relation to FM potential contributions. For further development a larger sample size of empirical data is need to be investigated in order to validate this exploratory paper.

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